

**IT 06-6**

**Tax Type: Income Tax**

**Issue: Withholding Tax – Failure to File Return/Make Payment**

**STATE OF ILLINOIS  
DEPARTMENT OF REVENUE  
OFFICE OF ADMINISTRATIVE HEARINGS  
SPRINGFIELD, ILLINOIS**

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**THE DEPARTMENT OF REVENUE  
OF THE STATE OF ILLINOIS**

**v.**

**JOHN DOE d/b/a ABC  
WOODWORKING and DOE’S HOUSE**

**Taxpayer**

**Docket No. 04-IT-0000  
FEIN 00-0000000  
Tax Years 1996--1999**

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**RECOMMENDATION FOR DISPOSITION**

Appearances: Kent Steinkamp, Special Assistant Attorney General, for the Department of Revenue of the State of Illinois; Mary E. Lopinot of Mathis, Marifian, Richter & Grandy, Ltd. for John Doe.

Synopsis:

The Department of Revenue (“Department”) issued a Notice of Deficiency to John Doe d/b/a ABC Woodworking and Doe’s House (“taxpayer”) for failing to file withholding tax returns for the years 1996 through 1999. The taxpayer timely protested the notice, and an evidentiary hearing was held. The taxpayer argues that he did not have to file withholding tax returns because he is not an employer within the meaning of the Illinois Income Tax Act. The two issues raised by the taxpayer are the following: (1) whether the taxpayer’s workers are employees for whom the taxpayer must withhold

taxes, and (2) if the workers are employees, whether the tax base should be reduced and the penalties and interest be waived. After reviewing the record, it is recommended that a portion of the liability be reduced.

FINDINGS OF FACT:

1. The taxpayer is a sole proprietor who is in the business of manufacturing wood cabinets and small buildings (e.g., gazebos, sheds, and playhouses). (Stip. #1, 2; Taxpayer Ex. D)

2. The taxpayer treated all workers as independent contractors for all tax periods at issue. (Stip. #6)

3. Several workers reported income received from the taxpayer on their individual federal and Illinois income tax returns for the relevant tax years. (Stip. #7)

4. The total amount of income reported by the workers referenced in the previous paragraph is \$35,695 for tax year 1997, \$99,183.35 for tax year 1998, and \$126,758.57 for tax year 1999. (Stip. #8)

5. The taxpayer received eight years of education from an Amish parochial school. He has not had any formal business training. (Tr. p. 8)

6. The taxpayer initially worked as a farmer. He later worked as a sausage maker, and then a woodworker. At the time of the hearing, the taxpayer was again working as a farmer. (Tr. p. 51)

7. In 1994 while the taxpayer was working as a sausage maker, two of his Mennonite friends, Mr. Jones and Mr. Smith, told him they wanted to get involved in woodworking. The taxpayer provided the capital for them, purchased all of the material, and rented the building in order for them to build kitchen cabinets and furniture. This

business was known as ABC Woodworking (“ABC”). The taxpayer continued to work in meat processing. (Tr. pp. 8-9)

8. The taxpayer’s initial investment in ABC was approximately \$50,000. All of the material that was used to manufacture the items was purchased with capital that the taxpayer had put into the business. (Tr. pp. 29-30)

9. The taxpayer provided the large items needed for the business. If an item was going to be used by all of the workers, such as a table saw, the taxpayer purchased it because it was not practical for the workers to bring their own table saw. These items included sanders, planers, forklifts, large saws, a vehicle, a trailer, and a dust collector. (Tr. pp. 12-15, 30, 44-45)

10. Mr. Jones and Mr. Smith had authority to use the business checking account to buy a new table saw or smaller items if there was enough money in the account and all the workers would use the items. (Tr. pp. 14-15)

11. The workers at ABC purchased their own hand tools and did not receive reimbursement from the taxpayer for the tools. Typical tools used at ABC included squares, levels, and measuring tapes. A lot of the Mennonite workers used their own cordless drivers. The Amish workers, however, could not own tools that used electricity, so they only brought tools that their religion allowed them to bring. (Tr. pp. 15, 44, 59-60)

12. The taxpayer subsequently purchased the building that was used by ABC. (Tr. p. 30)

13. Because the taxpayer invested capital into the business, once a month the taxpayer and his two friends would meet so that the friends could tell the taxpayer what

was happening in the business. The taxpayer would contribute additional capital when necessary. (Tr. pp. 12-13)

14. In late 1995, the taxpayer quit the sausage business and asked his two friends who were operating ABC if there was enough business to support three families if he worked with them. They indicated that there was not enough business. (Tr. pp. 10-11)

15. At that time, the taxpayer was more familiar with the construction of little storage buildings than kitchen cabinets, so he rented the building next door to ABC and started operating Doe's House ("House"). (Tr. pp. 10-11)

16. When the taxpayer started working at House, his son was the only other person who worked with him. In 1996 the taxpayer's friend, Mr. Brown, contacted the taxpayer about working at House and began working there. Mr. Brown began working at House in 1998. (Tr. pp. 11, 16-18, 53)

17. For House, the taxpayer provided the large capital items that were used to produce the buildings. He also provided all of the material for the buildings. The workers provided their own tools that they carry with them such as skill saws, hammers, and nail aprons. (Tr. p. 18)

18. If a customer called with a complaint about a cabinet or a building, the taxpayer would go to Mr. Jones, Mr. Smith, or Mr. Brown and ask them to explain why it was not manufactured correctly. (Tr. p. 37)

19. The workers for both ABC and House worked at buildings on ABC Lane in Anywhere, except when they were out on jobs to assemble the items that they built. (Tr. pp. 15, 19, 72)

20. The taxpayer took into consideration the amount that was spent on equipment to determine a percentage of income that would be spent on labor. (Tr. p. 45)

21. The taxpayer agreed with Mr. Jones and Mr. Smith to pay them 30% of the gross income from the cabinets for their compensation. (Tr. pp. 11-12, 24-25, 38)

22. The percentage that the taxpayer paid for labor did not change. Mr. Jones and Mr. Smith could hire workers to help build the cabinets, and the compensation for those workers was taken from the 30%. In other words, the amount of compensation that each individual received depended upon the number of workers who worked there and the number of cabinets that were built. (Tr. pp. 25-26, 38-39)

23. The agreement that the taxpayer made with Mr. Brown was that he was paid a percentage of the income received from the buildings that he built. (Tr. pp. 16-18)

24. The agreement that Mr. Brown made with the taxpayer was that Mr. Brown would oversee the shop, and Mr. Brown was paid 22.5% of the income received for gazebos. He received 15% for buildings that were priced less than \$1,000, and 10% for buildings over \$1,000. For lighthouses he received 25%. (Tr. p. 53)

25. Mr. Brown initially hired the workers at House. When Mr. Brown began working there, he hired workers.<sup>1</sup> (Tr. p. 25)

26. The percentage that the taxpayer paid for labor stayed the same no matter how many workers Mr. Brown hired to help. The taxpayer produced the sales order for Mr. Brown, and then they “would hire however many workers that they needed in order to produce what [the taxpayer] sold.” (Tr. pp. 25-26, 54)

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<sup>1</sup> It is not clear from the record when Mr. Brown stopped working at House.

27. The taxpayer was not involved in the production of the cabinets at ABC and did not hire or fire the workers who helped Mr. Jones and Mr. Smith with the production of the cabinets. (Tr. pp. 12-13)

28. The taxpayer did not participate in decisions concerning the number of workers to hire or who to hire. (Tr. p. 18)

29. The taxpayer was never consulted before a new worker started. (Tr. p. 55)

30. At House, the group of workers in the shop decided whether to hire more workers. If they decided that they were under more pressure with the new orders that were coming in, the workers as a group decided to find someone to help them. (Tr. p. 54)

31. Usually if a worker did not blend in with the “team,” the team found ways to discipline the worker to the point where he would find work somewhere else. (Tr. p. 42)

32. During a typical week, there was an average of five workers at House, including Mr. Brown. (Tr. p. 62)

33. The workers did not receive an hourly wage *per se*, but they took an hourly draw that was based on the labor percentage. (Tr. p. 39)

34. The hourly draw depended on factors such as whether the worker was married and his ability to do the work. A married man received a higher amount of the money. The other workers participated in deciding what the hourly draw would be. (Tr. pp. 39, 58-59)

35. The workers were paid every week, and this was based on an estimate of what the compensation for the quarter was going to be. (Tr. pp. 63-64)

36. The compensation for the workers was determined at the end of each quarter. They would look at how much money there was from the percentage that the taxpayer

gave them, and that amount was divided among the workers. At the end of the quarter, the weekly checks were subtracted from the total compensation. (Tr. pp. 58-59, 63-64)

37. The taxpayer did not participate in deciding how the money was divided. (Tr. p. 59)

38. If someone did not show up for work on a day during the week, they did not get paid for that day. At the end of the quarter, the number of days that a worker did not show up for work was factored into the amount that he received. (Tr. pp. 66-67)

39. The taxpayer wrote the weekly checks that were given to the workers. (Tr. p. 68)

40. The payments to the workers came from the taxpayer rather than Mr. Jones, Mr. Smith, or Mr. Brown because it was more convenient for the taxpayer to have all of the checks written from the same account. At the end of the quarter, the taxpayer would go through the check stubs and write down the expenses for labor, material, and overhead. (Tr. pp. 24-25)

41. The taxpayer used one checking account for both businesses. The taxpayer would keep track of the expenses for each business by writing DOE or ABC on the checks. (Tr. p. 33)

42. At the end of each year, the taxpayer reported the income that the workers received on Form 1099. The 1099's show the employer as "ABC/Doe's House." The taxpayer did not withhold federal or state taxes for the workers. (Taxpayer Ex. C; Tr. pp. 26, 40)

43. The taxpayer did not set the work hours for the workers at ABC or House. The workers were told what time the taxpayer would be at the workshop in the morning

so that they would know when they could go to work. The workers were not given a certain number of hours per week that they had to work. (Tr. pp. 14, 18, 41-42)

44. Approximately two-thirds of the workers had a key to the building so they had the option of working late or working on Saturdays. The taxpayer did not allow the workers to work on Sundays. (Tr. p. 43)

45. The business would usually close by 5:00 p.m., but if the taxpayer was there it remained open, often until 9:00 p.m.<sup>2</sup> (Tr. pp. 43-44)

46. The taxpayer did not provide any benefits to the workers at either ABC or House. He did not provide vacation pay, health insurance or worker's compensation insurance. (Tr. pp. 13-14, 18, 25)

47. The taxpayer did not provide any training for the workers. (Tr. p. 56)

48. For approximately nine months during 1999, Ms. White worked as a secretary for the taxpayer. (Tr. pp. 26-27)

49. The taxpayer filed a Form 1099 for Ms. White. (Taxpayer Ex. C)

50. Mr. Red was a "dealer" for the taxpayer. He had a sales lot where he sold items such as lawn furnishings, and he allowed the taxpayer to put his buildings on the lot. Mr. Red received a commission from the taxpayer when he sold a building. (Tr. p. 21)

51. Mr. Green, XYZ Nursery, and Mr. Blue also worked as dealers for the taxpayer. (Tr. pp. 21-22)

52. Mr. Orange was a driver for the taxpayer who delivered the buildings once they were sold. He did not work at the construction facilities. He received a percentage of the cost of the building. (Taxpayer Ex. C; Tr. pp. 23-24)

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<sup>2</sup> It is not clear from the record when the taxpayer stopped working at House.



53. The taxpayer filed a Form 1099 for the dealers and his driver. (Taxpayer Ex. C)

54. The taxpayer had stored his business records for the audit period in boxes in the attic of his home. In 2002, a tornado destroyed most of his home, and most of his records were lost. (Tr. pp. 27-28)

#### CONCLUSIONS OF LAW:

Section 701(a) of the Illinois Income Tax Act requires an employer maintaining an office or transacting a business within this State to withhold tax on compensation paid to an individual. 35 ILCS 5/701(a). The Department's regulations define compensation as remuneration for personal services performed by an "employee." See 86 Ill. Admin. Code, ch. 1, §100.3100(b). "The term 'employee' includes every individual performing services if the relationship between him and the person for whom he performs such services is the legal relationship of employer and employee. The term has the same meaning under the Illinois Income Tax Act as under 26 U.S.C. Section 3401(c) and 26 CFR 31.3401(c)-1." *Id.*

The Code of Federal Regulations provides in part as follows:

"Generally the relationship of employer and employee exists when the person for whom services are performed has the right to control and direct the individual who performs the services, not only as to the result to be accomplished by the work but also as to the details and means by which that result is accomplished. That is, an employee is subject to the will and control of the employer not only as to what shall be done but how it shall be done. In this connection, it is not necessary that the employer actually direct or control the manner in which the services are performed; it is sufficient if he has the right to do so. The right to discharge is also an important factor indicating that the person possessing that right is an employer. Other factors characteristic of an employer, but not necessarily present in every case, are the furnishing of tools and the furnishing of a place to work to the individual who performs the services." 26 C.F.R. §31.3401(c)-1(b).

Revenue Ruling 87-41 sets forth 20 factors to consider in determining whether sufficient control is present to establish an employer/employee relationship. The factors are as follows:

1. **Instructions.** Ordinarily an employee must comply with the employer's instructions about when, where, and how he is to work. This control factor is present if the person for whom the services are performed has the RIGHT to require compliance with instructions.
2. **Training.** Training indicates that the person for whom the services are performed wants the services performed in a particular manner.
3. **Integration.** Integration of the worker's services into the business operations generally shows that the worker is subject to direction and control. When the success or continuation of a business depends to an appreciable degree upon the performance of certain services, the workers who perform those services must necessarily be subject to a certain amount of control by the owner of the business.
4. **Services rendered personally.** If the services must be rendered personally, presumably the person for whom the services are performed is interested in the methods used to accomplish the work as well as in the results.
5. **Hiring, supervising, and paying assistants.** If the person for whom the services are performed hires, supervises, and pays assistants, this generally shows control over the workers. However, if one worker hires, supervises, and pays the other assistants pursuant to a contract under which the worker agrees to provide materials and labor and under which the worker is responsible only for the attainment of a result, this factor indicates an independent contractor status.
6. **Continuing relationship.** A continuing relationship generally indicates an employer/employee relationship. A continuing relationship may exist where work is performed at frequently recurring although irregular intervals.
7. **Set hours of work.** The establishment of set hours of work is a factor indicating control.
8. **Full time required.** If the worker must devote substantially full time to the business, the person who runs the business has control over the amount of time the worker spends working and impliedly restricts the worker from doing other gainful work.
9. **Doing work on employer's premises.** If the work is performed on the premises, this suggests control over the worker, especially if the work could be done elsewhere. The importance of this factor depends on the nature of the service involved and the extent to which an employer generally would require that employees perform such services on the employer's premises.

10. **Order or sequence set.** If a worker must perform services in the order or sequence set by the person for whom the services are performed, this shows that the worker is not free to follow the worker's own pattern of work but must follow the established routines and schedules of the person for whom the services are performed. It is sufficient to show control if the person for whom the services are performed retains the right to do so.
11. **Oral or written reports.** A requirement that the worker submit regular or written reports to the person for whom the services are performed indicates a degree of control.
12. **Payment by hour, week, month.** Payment by the hour, week, or month generally points to an employer/employee relationship, provided that this method of payment is not just a convenient way of paying a lump sum agreed upon as the cost of a job. Payment made by the job or on straight commission generally indicates that the worker is an independent contractor.
13. **Payment of business and/or travel expenses.** If these expenses are paid, the worker is ordinarily an employee. An employer, to be able to control expenses, generally retains the right to regulate and direct the worker's business activities.
14. **Furnishing of tools and materials.** The fact that the person for whom the services are performed furnishes significant tools, materials, and other equipment tends to show the existence of an employer/employee relationship.
15. **Significant Investment.** If the worker invests in facilities that are used by the worker in performing services, this tends to indicate that the worker is an independent contractor. On the other hand, lack of investment in facilities indicates dependence on the person for whom the services are performed and, accordingly, the existence of an employer/employee relationship.
16. **Realization of profit or loss.** A worker who can realize a profit or suffer a loss as a result of the worker's services (in addition to the profit or loss ordinarily realized by employees) is generally an independent contractor, but the worker who cannot is an employee. For example, if the worker is subject to a real risk of economic loss due to significant investments or a bona fide liability for expenses, such as salary payments to unrelated employees, that factor indicates that the worker is an independent contractor. The risk that a worker will not receive payment for his or her services, however, is common to both independent contractors and employees and thus does not constitute a sufficient economic risk to support treatment as an independent contractor.
17. **Working for more than one firm at a time.** If a worker performs more than de minimus services for a multiple of unrelated persons or firms at the same time, that factor generally indicates that the worker is an independent contractor. However, a worker who performs services

for more than one person may be an employee of each of the persons, especially where such persons are part of the same service arrangement.

18. **Making service available to general public.** The fact that a worker makes his services available to the general public on a regular and consistent basis indicates an independent contractor relationship.
19. **Right to discharge.** The right to discharge a worker is a factor indicating that the worker is an employee and the person possessing the right is an employer. An independent contractor, on the other hand, cannot be fired so long as the independent contractor produces a result that meets the contract specifications.
20. **Right to terminate.** If the worker has the right to end his relationship with the person for whom the services are performed at any time he wishes without incurring liability, that factor indicates an employer/employee relationship. Rev. Ruling 87-41.

If a taxpayer fails to file a return, the Department determines the amount of tax due according to its best judgment and information. 35 ILCS 5/904. The findings of the Department concerning the correct amount of tax due are *prima facie* correct, and the Department's certified record relating to the tax due is proof of such determination. 35 ILCS 5/904, 914; Balla v. Department of Revenue, 96 Ill. App. 3d 293, 295 (1st Dist. 1981). The taxpayer must produce sufficient credible evidence to the contrary to overcome the Department's *prima facie* case. Balla at 295.

The taxpayer has several different types of workers who must be considered as to whether they are employees or independent contractors. One is Ms. White, who worked as a secretary for the taxpayer. The taxpayer was asked during his direct testimony if any worker payments were reported on anything other than a 1099. He responded by stating that during a brief period he hired a secretary, and he introduced her to his accountant. He testified that he asked the accountant to make sure that he was doing things right, and then he stated, "I believe that there might have been some payments made as per what that accountant had recommended." (Tr. pp. 26-27) When he was asked during cross-

examination whether withholding taxes were taken out of the workers' checks he said, "Not that I'm aware of. Unless it was in that brief period of time when we had a secretary and she was working with the accountant." (Tr. p. 40) There was no other evidence indicating that payments were reported on anything other than the 1099s, and there was no other evidence concerning the services that Ms. White provided.

The 1099s that the taxpayer submitted for 1999 included one for Ms. White showing income of \$5,504. (Taxpayer Ex. C) The taxpayer has not suggested or indicated in any way that her secretarial services should be considered to be those of an independent contractor. Because the taxpayer has the burden of proving that the Notice of Deficiency is not accurate and the taxpayer has failed to present evidence showing that Ms. White was anything other than an employee, the taxpayer should have withheld taxes from her income.

The next worker who must be considered is the taxpayer's driver, Mr. Orange. The evidence indicates that he delivered the buildings once they were sold, and he received a percentage of the cost of the buildings. The taxpayer gave him a 1099 for 1999 showing income of \$10,809. Although it was not specifically stated, Mr. Orange apparently drove the pickup truck that was purchased by the taxpayer. The taxpayer did not provide any other evidence concerning the duties of the driver and has not argued that he should be considered to be an independent contractor. From the little amount of evidence that was presented concerning Mr. Orange, it must be concluded that he was an employee and not an independent contractor.

Other workers to be considered include Mr. Jones, Mr. Smith, Mr. Brown, and Mr. Brown. These are the workers who had direct contact with the taxpayer and were

responsible for hiring other workers. First, it is not clear from the record if the taxpayer continued working for House when Mr. Brown was hired, and it is possible that the taxpayer supervised his activities while working there. Nevertheless, even if the taxpayer did not personally direct the manner in which these workers performed their services, the taxpayer described his relationship with these men as a “partnership.” (Tr. p. 29) He said, “They would do one aspect of it and I was responsible for another aspect of it.” *Id.* During the hearing, Mr. Brown stated, “I consider myself to be shop manager.” (Tr. p. 56) When a customer had a complaint about one of the products, the taxpayer went to these men to discuss the problem. The taxpayer testified that House “has a certain amount of name recognition,” and one of its buildings “will bring a premium because the people know that’s a quality business.” (Tr. p. 17) Although the taxpayer did not give specific instructions, he had the right to require compliance with the sales orders and presumably had the right to discharge these workers if they did not perform to the taxpayer’s satisfaction. Their services were integrated into the business operations, and they maintain a continuing relationship with the taxpayer.

With respect to ABC, the taxpayer met with Mr. Jones and Mr. Smith on a regular basis to receive oral reports as to how the business was performing. As for House, the taxpayer initially worked there himself and hired his son to work for him. Because it is not clear from the record when the taxpayer stopped working there, it cannot be determined at what point someone else was responsible for supervising the daily activities. Nevertheless, considering the significant amount of capital that the taxpayer invested into House, it is reasonable to conclude that he received regular reports concerning the progress of the business.

There are other factors that indicate that all of the workers who constructed the products were employees rather than independent contractors. The taxpayer provided all of the capital for the businesses. He purchased all of the equipment used to produce the products, and he provided the materials for the products. The workers brought their own hand tools, but the taxpayer was responsible for making sure there were enough supplies. (Tr. p. 75) The fact that the workers provided small tools is not a significant factor. See United States v. Silk, 331 U.S. 704, 717-718 (1947). Mr. Brown testified that the taxpayer established his policy concerning supplies by giving Mr. Brown two new brooms and saying that he would replace the brooms if they wore out, but if Mr. Brown broke the handle, Mr. Brown would buy the new broom. (Tr. p. 76). Thus, the taxpayer provides the supplies, materials, and equipment for the businesses.

The fact that the taxpayer does not establish or set the hours of work is also not determinative. See Silk, *supra*. Mr. Brown made reference to the fact that he sometimes works other jobs (Tr. p. 56), but he did not say how much of his time is spent doing that. It is not clear how often the other workers do that as well. Given the amount of work that they do and the fact that they sometimes work late and on Saturdays, it appears as though the workers devote a substantial amount of their time to the taxpayer. All of the work, except for the installation of the products, is done on the taxpayer's premises. The workers do not own or rent the premises, and they do not own any of the significant capital equipment. Because the workers are given the purchase orders from the taxpayer, the work must presumably be performed in the order in which the requests are made. When the taxpayer was asked whether there was a distinction between the workers and those he considered to be "partners," he explained that he would go to the partners if the

customers had complaints about the product, but otherwise “there was no difference in my mind.” (Tr. p. 37) He said that when he looks at the workers, “they are on the same page with me.” *Id.*

The taxpayer controls all meaningful aspects of the business relationship. The workers do not have control over the prices charged; they make the products for the taxpayer’s customers and for the price set by the taxpayer. They have no input concerning the quantity or price and do not have a choice as to who to sell to. The taxpayer directly pays all of the workers. Although the amount of money that the workers make depends on the number of products that they build, they do not actually realize a profit or loss. Their profit is simply wages paid for the products built. The evidence supports a finding that these workers are employees of the taxpayer.

The final group of workers to consider is the dealers who sell the taxpayer’s products. The dealers are their own businessmen and operate their own businesses. They sell the taxpayer’s products and receive a commission for each item sold. The taxpayer has no control over their operations. This evidence indicates that the dealers are independent contractors rather than employees. Nevertheless, the only evidence presented concerning the amount of money paid to the dealers is one 1099 to Mr. Red for 1999 for \$19,982.27. (Taxpayer Ex. C) Although the taxpayer was not required to withhold taxes for this amount, the taxpayer has failed to meet its burden of showing the amount of income paid to the other dealers during the years in question.

The taxpayer argues that if it is determined that he is an employer within the meaning of the Act, the taxable base for the periods in question should be reduced by the amount of income that was individually reported by each of the workers. The parties



stipulated that these amounts are \$35,695 for tax year 1997, \$99,183.35 for 1998 and \$126,758.57 for 1999. (Stip. #8) The taxpayer contends that the purpose of the withholding provisions is to ensure the payment of taxes from an individual taxpayer. The taxpayer claims that if the individual has paid all of his tax liability independent of the withholdings, then the State has not been harmed by the failure to withhold.

Section 706 of the Act provides as follows:

Employer's Failure to Withhold. If an employer fails to deduct and withhold any amount of tax as required under this Act, and thereafter the tax on account of which such amount was required to be deducted and withheld is paid, such amount of tax shall not be collected from the employer, but the employer shall not be relieved from liability for penalties or interest otherwise applicable in respect of such failure to deduct and withhold. 35 ILCS 5/706.

Because this provision allows relief for the amount of tax that was paid, the portion of the liability must be reduced by the amounts stipulated to by the parties.

The taxpayer also argues that the penalties and interest in this matter should be waived if the workers are found to be employees. The taxpayer states that he is an unsophisticated taxpayer with an Amish eighth-grade education and has no formal training in business and tax management. He contends that he engaged the services of a tax professional to advise him, and he relied on that advice. He maintains that he acted reasonably and without the intent to circumvent the withholding provisions of the Act.

With respect to the interest there is no provision in the Act that allows the interest to be waived. An agency only has authority given to it by the legislature through the statute. Davis v. Chicago Police Board, 268 Ill. App. 3d 851, 856 (1st Dist. 1994). Because there is no statutory authority to abate the interest, it cannot be recommended that it be waived.

The penalties may be abated if the taxpayer establishes "reasonable cause" for the failure to file the tax returns. See 35 ILCS 735/3-8. The Department's regulation concerning reasonable cause provides in part as follows:

"The determination of whether a taxpayer acted with reasonable cause shall be made on a case by case basis taking into account all pertinent facts and circumstances. The most important factor to be considered in making a determination to abate a penalty will be the extent to which the taxpayer made a good faith effort to determine his proper tax liability and to file and pay his proper liability in a timely fashion." 86 Ill.Admin.Code §700.400(b)

The Department's regulation further states that a taxpayer is considered to have made a good faith effort to determine and file and pay his proper tax liability if he exercised ordinary business care and prudence in doing so. 86 Ill.Admin.Code §700.400(c). This depends on the clarity of the law or its interpretation, and the taxpayer's experience, knowledge, and education. *Id.* "[R]eliance on the advice of a professional does not necessarily establish that a taxpayer exercised ordinary business care and prudence." *Id.*

The evidence is not clear as to when the taxpayer went to his accountant to seek advice regarding the withholding taxes. It appears as though it may not have happened until 1999 when he took his secretary to the accountant, and even then it is not exactly clear what the accountant told him. Nevertheless, the taxpayer's background includes a small amount of education and no business experience. Considering the taxpayer's knowledge and education, I believe that the penalties should be abated.

Recommendation:

For the foregoing reasons, it is recommended that the basis of the tax liability be reduced by the amount of income paid to the dealer, Mr. Red, of \$19,982.27. It should also be reduced by the amount of income on which taxes were paid, which the parties

stipulated to be \$35,695 for tax year 1997, \$99,183.35 for 1998 and \$126,758.57 for 1999. Finally, it is recommended that the penalties be abated.

Linda Olivero  
Administrative Law Judge

Enter: May 2, 2006